CONCEPT: SUBSIDIES

● A ***subsidy*** is money paid by the government to market participants. It is effectively a “reverse-tax.”

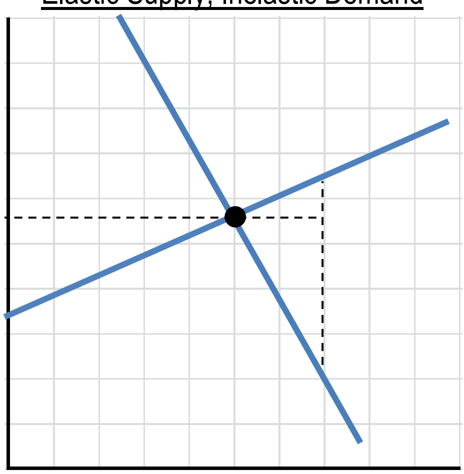
□ Our conclusions remain similar:

- The party receiving the subsidy does not necessarily get the full benefit of the subsidy payment.
- The split of the benefits depends on the price elasticities of supply and demand.
- Subsidies cause deadweight loss from *over-trading*

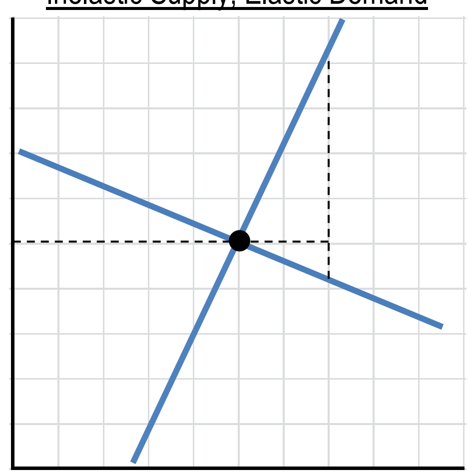
□ However, these ideas are different:

- The subsidy shifts the curve of the party receiving the money to the ___________ by the subsidy amount.
- P_b and P_s are inverted. Now, the amount buyers pay is less than the amount sellers receive.

Elastic Supply, Inelastic Demand



Inelastic Supply, Elastic Demand



□ The curve that is more inelastic represents the group who will receive ______________ subsidy benefit.

- Demand Curve more inelastic →
- Supply Curve more inelastic →

□ Whoever pays more tax (i.e. more inelastic), gets more subsidy benefit (i.e. more inelastic)

PRACTICE: A government wants to increase the use of solar panels by offering a $100 subsidy for each solar panel purchased. The addition of this subsidy will:

a) Increase the quantity supplied
b) Decrease the quantity supplied
c) Create a deadweight loss in the market for solar panels
d) Both (a) and (c)

PRACTICE: The government wants to help producers of a life-saving machine, so they introduce a $1,000 subsidy per machine produced. Assuming that demand for this machine is inelastic, the subsidy will:

a) Increase the price paid by consumers by $1,000
b) Increase the price paid by consumers by less than $1,000
c) Decrease the price paid by consumers by less than $1,000
d) Have no effect on the price paid by consumers